IN THE

Supreme Court of the United States

OCTOBER TERM, 1943

No. 3.

A. M. ANDERSON, RECEIVER OF THE NATIONAL BANK OF KENTUCKY, OF LOUISVILLE, *Petitioner,*

v.

KATHERINE KIRKPATRICK ABBOTT, ADMINISTRATOR, ET AL., *Respondents.*

SUPPLEMENTAL RECORD REFERENCES RE CALDWELL.

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PRESS OF BYRON S. ADAMS, WASHINGTON, D. C.

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Upon reargument, respondents devoted considerable time to the unconsummated negotiations between Banco Kentucky Company and Caldwell & Company. It was stated that this abortive deal was evidence of Banco's original purpose to engage primarily in the investment banking field. From this premise respondents argued that Banco's double assessment bank stock holding was only incidental to its original and main purpose of investment banking. The record in this case completely destroys any such argument.

1. Consolidation or partnership between Banco and Caldwell was never even thought of when Banco was organized. The agreement was made May 28, 1930, a few months before the collapse (R. 1, p. 258). Consequently it could not have been one of the original or "avowed purposes" of Banco.

2. The "Caldwell deal" was not a good faith effort of Banco to engage in investment banking. It was, as the court found, never "consummated". (R. 1, p. 262). As one of the directors testified, it was nothing but an attempt to "swap" four hundred thousand shares of "worthless" Banco for ten thousand shares of "worthless" Caldwell stock (R. 3, p. 103).

3. The "Caldwell deal" was merely another one of a series of unconsummated proposals to which publicity was given in an effort to avert inevitable failure.

The formation of the BancoKentucky holding company was proposed to the bank examiner to induce him to waive the charge-off of losses (Exhibit V-2, p. 612). Subscriptions to the stock of BancoKentucky were payable October 1, 1929. On that very day, Mr. Vaughn, an attorney, was employed to denationalize the National Bank of Kentucky and change it over to a state bank (R. 3, p. 25). This proposal was publicized and used to induce the bank examiner to again waive charge-offs. After it had served the purpose, the proposal to denationalize, which was continued as a pending proposal from October 1929 to March 1930, was abandoned (Ex. V2, p. 1024).

Another publicity move to bolster failing public confidence was the announcement that the National Bank of Kentucky would move into a beautiful new bank building at 421 Market Street. (Ex. V3, p. 1197) This was printed with a picture of the building, in the newspapers (Ex. V3 p. 1225). The Bank of Kentucky never moved into the bank building at 421 Market Street. See *National Bank of Kentucky* v. *Louisville Trust Co.*, 67 F.(2d) 97; *Louisville Trust Co.* v. *National Bank of Kentucky*, 102 F.(2d) 137.

Another proposal, never consummated, was a physical merger of the National Bank of Kentucky and the Louisville Trust Company. (R. 3, p. 172)

The deal with Caldwell was in character with the above proposals. It was immediately publicized (June 2, 1930) by President Brown of Banco as "by far the largest and most important financial structure ever built in the midwestern or southern states and one that will undoubtedly stand out in the future as one of America's greatest financial institutions." (See brief for respondents, p. 20)

Having been publicized as above, no further effort was made to complete any appraisal of Caldwell's assets on which the deal was entirely contingent (R. 3, p. 273) and, on November 6, 1930, President Brown could therefore truthfully announce that "negotiations * * * have never been consummated. The BancoKentucky Company is, therefore, *not connected in any way with the affairs of Caldwell and Company.*" (See brief for respondents, p. 21).

The unconsummated contract between Caldwell and Company and BancoKentucky (R. p. 258) shows that it was merely a paper deal. No money was invested by either party. BancoKentucky had previously increased its authorized capital stock from two million shares to five million shares (Ex. V3, p. 1086). Under paragraph 1 of the contract, the bankrupt Caldwell Company agreed to increase its authorized capital stock from ten thousand shares to twenty thousand shares; then Banco agreed to exchange nine hundred thousand shares of its "presently authorized, but unissued stock" for ten thousand shares of Caldwell.

Although the contract says nine hundred thousand shares, it was four hundred thousand, because four hundred thousand Banco shares were placed in escrow with the Trust Company "pending such examinations and investigations as the first party (Banco) may desire to make under Sections 7 and 8 of this agreement." By side agreement, one hundred thousand shares were supposed to be used to wash out the worthless paper of the Kentucky Wagon Works held by

the National Bank of Kentucky (R. 3, pp. 27, 100). Banco covenanted that it was a bank stock holding company and that its assets were the banks set forth in Section 6 (R. 1, p. 260). Caldwell falsely represented that it had a net worth of $9,000,000 but Banco was to have one year from May 28, 1930, to "satisfy itself as to the valuation". (R. 1, p. 261).

The making of the contract one year after the organization of Banco and a few months before BancoKentucky's failure and the exchange of some "worthless paper", was all that was ever done. No steps were ever taken to carry out the terms of the agreement. No valuation of Caldwell's assets, upon which the whole agreement was contingent, was ever made or even attempted. (R. 2, p. 295; R. 3, p. 274). The most convincing proof that the deal was a mere paper transaction, intended for publicity purposes on the part of both Caldwell and Brown, is that not one dollar of dividends was ever paid to Caldwell on the Banco stock supposedly issued to Caldwell. From May 28, when the contract was made, until the failure of BancoKentucky and Caldwell a few months later, two dividends were declared and paid by the BancoKentucky Company. Although BancoKentucky stock stood in the name of Caldwell and Company, the dividends paid to all other stockholders were not paid to Caldwell—because there was in fact no *bona fide* deal and it was not intended to part with any money.* (R. 1, p. 303; Stipulation of Facts, R. 2, p. 105).

Mr. Allen Dodd, counsel for respondents, and director, testified:

> "Q. In your experience as a lawyer and director of a bank, would you say that the Caldwell & Co. contract was consummated?

* Donovan, secretary of Caldwell, testified that they were not entitled to dividends because no examination of the assets of Caldwell had been completed. The first dividend check was endorsed back to Banco and "the next quarterly dividend came in September, 1930. I don't recall that a check was issued to us for that dividend. My recollection is that a check was not issued. We received no part of the September, 1930, dividend." (R.1, p. 303)

"A. Of course, the contract was not consummated on its terms as written, but let me be plain on the proposition. When I left the Board of Directors' meeting on May 26, it was thoroughly understood that the only contract to be made with Caldwell & Co. was to be a scale contract *and nothing was to be done until after the securities were valued. I did not think a contract would ever be drawn. When I got back to Louisville, I understood nothing had been delivered.* • • •

"It was my understanding that the purchase price would be held by BancoKentucky until after its own appraisement so that if the assets proved to be of no value it would not have to be delivered. • • • BancoKentucky never made any appraisement or audit of the assets of Caldwell & Co., and never paid any dividends on the stock allocated to Caldwell in the deal, that I know of. I think I have checked the records and found that to be true." (R. 2, pp. 293, 295.)

Mr. T. Kennedy Helm, counsel for defendants and a director, testified:

"That deal with Caldwell was completed without our Board or myself having any other knowledge of what Caldwell's assets were than what Mr. Brown told us Caldwell had told him. (R. 3, p. 99)

• • •

"According to Mr. Brown, Caldwell had refused to have an audit made until the trade was agreed upon because he did not wish to submit his private papers to outsiders until the trade was consummated. And the trade would not be consummated in full until there was an audit. Th stock was held in escrow pending adjustment from the audit. (R. 3, p. 100)

• • •

"My recollection is that 400,000 shares of the 800,000 shares were taken back. As to the 400,000 shares Caldwell held, dividends were not to be paid on them until it was sold and there was an audit." (R. 3, p. 101)

Respondent E. Leland Taylor, a director, testified:

"I was one of the men who voted to make this deal with Caldwell. I was for him, I guess I voted for him. *It*

was my understanding that that contract had a year in which we were to evaluate the assets of Caldwell. I did not figure in my mind that the contract was binding until the appraisal was made. If Caldwell & Co.'s assets proved to be nothing, there was to be no payment and no contract consummated. In other words, the contract was a contract to buy rather than having bought. Caldwell's assets were to be so much, but if it was less we would pay less, and if it proved to be more, we would pay more. If it were nothing, we would pay nothing.

"The appraisal of Caldwell's assets was never made. He had a year, and during that year he was to specify when he was ready to have the appraisal made and before that year ended, things blew up and it never was made. Some stock was turned over to Caldwell. No dividends were paid on it. We did not know it was going to be turned over and I suppose it was." (R. 3, pp. 273, 274)

4. Any argument that investment banking was an original or primary purpose of Banco is precluded by sworn statements of its officers, duly authorized by its directors (V. 3, pp. 1072, 1075, 1103), filed with the State of Delaware (Ex. V. 4, p. 1921a), and with the stock exchanges in Chicago (Ex. V. 4, pp. 1711, 1723) and Louisville (Ex. V. 4, p. 1695) (quoted in Receiver's main brief pp. 37, 43), which state that its sole purpose was to hold, operate and control banks and trust companies; and by the positive and very truthful written statement of its secretary that it did not intend to go in the investment banking business.

"This company has not engaged in the business of investing and reinvesting in a diversified list of securities of other corporations for revenue and profit but has limited its activities to acquiring control of banks and trust companies and the operation of same." (Ex. V. 4, p. 1713)

5. That the sole purpose of Banco was holding assessable bank stock is made crystal clear by the sworn testimony of respondents who were directors of the bank and Banco and

attorneys for themselves and other respondents. Director Dodd, a member of the common board of the bank and trust company and trustee under the April 22 trust agreement and a director of Banco, testified:

> "The primary purpose of the organization of Banco-Kentucky Company was to acquire a group of banks in the Ohio Valley." (R. 2, p. 261)

Director Carroll, who prepared the articles, testified:

> "Q. What was the purpose of the organization of the BancoKentucky Company?
> "A. Just as stated in that charter, to acquire stock in these other institutions as a holding company.
> "Q. As a holding company its primary purpose was to own and control a chain of banks?
> "A. Yes. I think that was the reason." (R. 3, p. 153)

Director Speed testified that:

> "The main object of the formation of the Banco-Kentucky Company (was) to acquire a chain of banks." (R. 3, p. 188)

Director Hiatt testified that the,

> "* * * purpose of the organization of BancoKentucky Company * * * was for control of the banking situation in the Middle West." (R. 3, pp. 202-203)

Director Boomer considered the organization of Banco as a means of

> "* * * extension of our interest in the other banks, such as the Covington bank and Cincinnati banks and Paducah, etc., that we afterwards purchased." (R. 3, p. 245)

Director Horace Taylor testified:

> "It was well known to me and to my fellow directors that the primary purpose of this institution was to first secure a majority of the National Bank of Kentucky stock and the Louisville Trust Company stock as a

nucleus for a group of banks in the Ohio Valley." (R. 3, p. 252)

6. What Banco's intentions were can best be gleaned by what it actually did in the short period of its existence. The only thing it ever did was to hold assessable bank stocks.

7. The only thing in the whole record even hinting that Banco had a purpose or intention beyond holding assessable bank stocks is the self-serving testimony of some of its directors, in a feeble effort to conjure up a defense to this case, to the effect that there was a vague intention, some time in the future, to engage in investment banking. Such testimony contradicts the written, sworn statements of its officers filed with the Secretary of State of Delaware and with the stock exchanges, and is contradicted by the testimony of the same directors as to what Banco actually did. Compare Dodd R. 2, p. 227 with R. 2, p. 261. Compare Helm R. 3, p. 53 with R. 3, pp. 79, 81.

8. Even if some of the respondents had investment banking in mind, we submit that such intention (never carried out) is of no avail to relieve shareholders of a company, primarily designed and intended to own banks and bank stocks, from assessment liability imposed by federal statute. The bank holding companies in Detroit and elsewhere actually engaged in investment banking through First National Detroit Company, The Detroit Company and The Assets Realization Company in *Barbour* v. *Thomas*, 86 F. (2d) 510,* and through Keane Higbee Company in *Deming* v. *Schram*, 7 F. Supp. 271.** Such activity, it was held, did not relieve the shareholders from assessment liability, since the main purpose was to control the banks and to pass

* See transcript record on file with clerk this court, No. 718, October Term 1936, V. 3, Ex. 97, pp. 1097, 1121; Ex. 99A p. 1193; Ex. 99B, p. 1210; Ex. 101A, p. 1267; Ex. 101B, p. 1272.

** See Ex. V. 5, p. 2171, 2181-2.

on the dividends received from bank stocks to the shareholders of the holding company.

9. Banco was incorporated July 1929 but it did no business until September 25, 1929. It then made a contract to buy the stock of two Cincinnati banks, both assessable under Ohio statutes, for Seven Million Dollars (R. 2, pp. 262, 280). Subscriptions to Banco were not payable until October 1, 1929. It would require substantially all of this subscription money to pay for the Cincinnati bank stocks. So from the beginning to the end Banco never had any substantial assets with which to pay an assessment on a bank stock except other assessable bank stock.

10. The above statements would be true even if we were to consider the belated and unconsummated Caldwell deal as an accomplished fact. There is a stipulation in the record that Caldwell was insolvent as of May 31, 1930 (the contract was dated May 28, 1930) to the tune of $1,111,170.30 (R. 2, p. 105). Creditors of Caldwell only received a dividend of one-tenth of one per cent (R. 2, p. 106); an infinitesimal amount with which to pay bank stock assessments. Besides, Caldwell was quite a bank stock holding company in its own right. It controlled directly, and through its controlled insurance companies, the assessable stock of sixty-six other banks and trust companies.***

11. Finally, BancoKentucky Company was a Delaware Company and was legally incapacitated by the Kentucky Constitution and statutes then in effect from transacting investment banking, title insurance or making mortgage loans in Kentucky. It never qualified to do any business in that state (Ex. V. 4, p. 1693), (Kentucky Stat. § 571). Nor did it file a report or pay the license tax required by Kentucky Statute 4189-2 (Ex. V. 4, p. 1694).

*** See table compiled from Federal Reserve data by Cartinhour —Branch, Group and Chain Banking, p. 66; Caldwell's original suggestion for the consolidation: "I have been wondering lately whether it would be feasible to consider a consolidation between the Banco Kentucky Corporation and the banks in which we are interested." (Ex. V. 4, p. 1840); Ex. V. 3, p. 1207.

The Kentucky Constitution, §202, contains the following prohibition:

> "No corporation organized outside the limits of this state shall be allowed to transact business within the state on more favorable conditions than are prescribed by law to similar corporations organized under the laws of this commonwealth."

BancoKentucky was not subject to the supervision of the Banking and Securities Department of Kentucky. §165a-1 of Kentucky statutes makes this mandatory with respect to "banks, trust companies, savings banks, combined banks, real estate mortgage companies."

The nine lawyers, members of Banco's board, knew that the provision that Banco shares should be "non-assessable" made it legally impossible for BancoKentucky Company to engage in investment banking or title insurance in the State of Kentucky. §547 Kentucky Statutes provides:

> "Stockholder in guaranty companies, investment companies and insurance companies shall be liable equally and ratably, and not one for the other, for all contracts and liabilities of such corporation to the extent of the amount of their stock at par value, in addition to the amount of such stock."

Respondents can hardly be heard in a court of equity to say that they had an original purpose to violate the laws of Kentucky or to do business prohibited there to foreign and domestic corporations.

Respectfully submitted,

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